PT 98-2
Tax Type: PROPERTY TAX
Issue: Charitable Ownership/Use

STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS

KATHERINE MANOR LIMITED PARTNERSHIP, APPLICANT	**Nos. 94-22-239 and 94-22-046 through & including 94-22-050**
	Real Estate Tax Exemptions for 1994 Assessment Year
v.	**P.I.N.S: 08-08-113-022 08-08-113-001 08-08-113-010 08-08-113-016 08-08-113-018 08-08-113-027**
	DuPage County Parcels
ILLINOIS DEPARTMENT OF REVENUE	**Alan I. Marcus, Administrative Law Judge**

RECOMMENDATION FOR DISPOSITION

APPEARANCES: Mr. J. Randolph Given of on behalf of Katherine Manor Limited Partnership; Mr. Robert Rybica, Assistant State's Attorney for the County of DuPage on behalf of the DuPage County Board of Review.

SYNOPSIS: These proceedings raise the following issues: first, whether real estate identified by DuPage County Parcel Index Numbers 08-08-113-022, 08-08-113-001, 08-08-113-010, 08-08-113-016, 08-08-113-018 and 08-08-113-027[1] (hereinafter collectively referred to as the "subject properties" or the "subject parcels") qualify for exemption under Public Act 88-660, passed by the General Assembly on June 30, 1994 and effective September 16, 1994; and if they do not, whether such parcels satisfy the ownership and use requirements necessary to obtain exemption from 1994 real estate taxes under 35 **ILCS** 200/15-65.[2] In relevant part, that statute provides as follows:

> All property of the following is exempt [from real estate taxation] when actually and exclusively used for charitable or beneficent purposes, and not leased or otherwise used with a view to profit:
>
> (a) institutions of public charity.

The General Assembly amended Section 200/15-65 via enactment of Public Act 88-660. This provision, effective September 16, 1994, provides, in relevant part, that property otherwise qualifying for exemption under Section 200-15/65 shall not lose its exemption because the legal title is held:

> … (ii) by an entity that is organized as a partnership, in which the charitable organization, or an affiliate or subsidiary of the charitable organization, is a general partner, for the purposes of

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1. Each of the six Parcel Index Numbers begins with the same seven digits, to wit, "08-08-113." In the interest of administrative economy, I shall hereinafter refer to each parcel only by the last four digits of its Parcel Index Number. Thus, for example, Parcel Index Number 08-08-113-022 shall hereinafter be referred to as "022."

2. In People ex. rel. Bracher v. Salvation Army, 305 Ill. 545 (1922), the Illinois Supreme Court held that the issue of property tax exemption necessarily depends on the statutory provisions in force during the time for which the exemption is claimed. This applicant seeks exemption from 1994 real estate taxes. Therefore, the applicable provisions are those found in the Property Tax Code, 35 **ILCS** 200/1 *et seq*.

> owning and operating a residential rental property that has received an allocation of Low Income Housing Tax Credits for 100% of the dwelling units under Section 42 of the Internal Revenue Code of 1986.[3]

The controversy arises as follows:

On December 29, 1993, Katherine Manor Limited Partnership (hereinafter "KMLP" or the "applicant") filed six separate Applications for Property Tax Exemption[4] with the DuPage County Board of Review (hereinafter the "Board") (Dept. Group. Ex. No. 1, Docs. A through F).

The Board reviewed the applications and subsequently recommended to the Illinois Department of Revenue (hereinafter the "Department") that the all of the subject properties except parcel 022[5] be exempt. *Id*.

The Department later rejected most of these recommendations by issuing five certificates finding that parcels 001, 010, 027, 016 and 018 were not in exempt ownership. Dept. Group Ex. No. 2, Docs. B through F. It also issued a certificate finding that parcel 022 was neither in exempt ownership nor in exempt use. Dept. Group Ex. No. 2, Doc. A.

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3. 26 U.S.C.A. § 42.

4. The six applications were docketed as follows:

Docket Number	Corresponding P.I.N.
94-22-239	022
94-22-046	001
94-22-047	010
94-22-048	027
94-22-049	016
94-22-050	018

Dept. Group Ex. No. 1.

5. The Board specifically recommended that this particular parcel not be exempt. Dept. Group Ex. No. 1, Doc. A.

Applicant filed timely requests for hearing as to each of these denials (Dept. Group Ex. No. 3, Docs. A and B) and thereafter entered into an undated stipulation of facts with the DuPage County State's Attorney as authorized agent for the Board. Both parties then participated in a Pre-Trial Conference, at which time they submitted their stipulation and supporting documentation. At the conclusion of this Conference, the parties also signed a Pre-Trial Order which provided, *inter alia* that both parties: (1) expressly waived their respective rights to a formal evidentiary hearing; (2) would be bound by the stipulation of facts (Joint Ex. No. 1) and relevant supporting documentation (Joint Ex. Nos. 2 through 20) submitted therewith and (3) effectuate same by limiting the record to the stipulation and its supporting documentation.

Following submission of that stipulation and its supporting documentation, I recommend that the subject properties not be exempt from 1994 real estate taxes.

FINDINGS OF FACT:

1. The Department's jurisdiction over these matters and its positions therein, namely that parcels 001, 010, 027, 016 and 018 were not in exempt ownership during the 1994 assessment year, and further, that parcel 022 was neither in exempt ownership nor exempt use during same, are established by the admission into evidence of Dept. Group Ex. Nos. 1 and 2.

2. All of the subject parcels are located at 1141 Iroquois, Naperville, IL 60563. They are part of a two-story, 32 unit residential structure commonly known as Katherine Manor. Dept. Group Ex. No. 1; Joint Ex. No. 1.

3. Katherine Manor consists of 32 individual condominium units that are especially designed for people with physical disabilities. *Id*.

4. Each of the 32 units at Katherine Manor is owned by one of four groups of owners: (1) private individuals; (2) Illinois Independent Living Center, Incorporated (hereinafter

"IILC"), an Illinois not-for-profit corporation that is also exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code; (3) Katherine Manor Condominium Association (hereinafter "KMCA"), an Illinois not-for-profit corporation that is also exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code; and (4) applicant, an Illinois limited partnership. *Id*; Joint Ex. No. 12.

5. All units owned by private individuals are taxable and not at issue herein. *Id*.

6. The Department determined that the IILC-owned units, which are not at issue herein, were exempt from real estate taxation in Departmental Docket Nos. 92-22-203 through 208 and 92-22-210 through 92-22-215. The Department granted these exemptions on the basis that IILC qualified as an "institution of public charity" under the applicable statute and used the units in question for exempt purposes. Administrative Notice; Joint Ex. No. 1.

7. The Department further determined, via a Hearing Disposition in Docket Number 93-22-59, that one of the KMCA-owned units, identified by DuPage County Parcel Index Number 08-08-113-004, qualified for exemption from 1993 real estate taxes. The Department granted this exemption on grounds that KMCA qualified as an "institution of public charity" under the applicable statute and used the unit in question, which is not at issue herein, for exempt purposes. Administrative Notice; Joint Ex. No. 1.

8. Only the six units owned by KMLP are at issue in the present case. Said units are identified by the following Parcel Index Numbers:

P.I.N.	**Unit Number**
022	208
001	103
010	113
027	213
016	201
018	203

Id; Joint Ex. No. 1.

9. KMLP acquired ownership of the above units via six separate warranty deeds dated December 29, 1988. Each of the six deeds names IILC as grantor. Joint Ex. Nos. 1, 13.

10. Applicant was created pursuant to a limited partnership agreement (hereinafter the "Agreement") dated December 1, 1988. Its managing general partner is IILC, which is also the developer of Katherine Manor and the management agent for KMCA. Joint Ex. Nos. 1, 2 and 3.

11. KMCA was admitted as applicant's financial general partner in exchange for its transfer of ownership of two of the six subject properties. Joint Ex. No. 2.

12. IILC created applicant for the purpose of raising funds from a private investor for the acquisition and improvement of the subject properties under the Low Income Housing Tax Program administered by the Illinois Housing Development Authority. (hereinafter the "Authority").

13. IILC procured this investor, Midwest Electronics, Inc, (hereinafter "Midwest")[6] by executing a first amendment to the Agreement on January 31, 1989. Under terms of this amendment IILC, in its capacity as applicant's general partner: (1) approved an assignment of

6. The Stipulation did not make any mention of Midwest's organizational documents. Nor did the supporting documentation contain same.

99% of the limited partner's interest in the partnership to Midwest; (2) effectuated the same transaction and (3) admitted Midwest as a limited partner in KMLP. Joint Ex. No. 5.

14. The Low Income Housing Tax Credit Program originated in Section 42 of the Internal Revenue Code, 26 USC §42 (hereinafter the "Code"). Congress intended the tax credits provided in Section 42 of the Code to induce private entities to construct or rehabilitate housing for low and moderate income persons. Joint Ex. No. 1.

15. Each state is allocated approximately $1.25 in tax credits per person of population in the state for purposes of this program. The credits must be allocated. Under Section 42(m)(1)(B)(iii) of the Code, each state designates an agency to allocate and monitor the credits. *Id.*

16. The Authority is responsible for allocating and monitoring those credits in all regions of the State of Illinois except for the City of Chicago. *Id*.

17. Each entity receiving tax credits pursuant to the Low Income Tax Program receives the credits for a period of ten years, but must set aside units for low and moderate income tenants and are subject to rent restrictions for a period of 15 years. *Id*.

18. The Low-Income Housing Credit Schedules and Low-Income Housing Allocation Certifications (IRS Forms 8586 and 8609) attached to applicant's 1990, 1991 and 1992 federal income tax returns[7] indicate that KMLP claimed Low-Income Housing Credits for five of the six units. These credits were allocated as follows:

	1990	**1991**	**1992**
Unit Number			
103	$5,721.00	$5,721.00	$5,721.00
113	$5,702.00	$5,702.00	$5,702.00
201	$5,817.00	$5,817.00	$5,817.00

7. The stipulation made no mention of applicant's 1994 federal income tax return. Nor did any of the supporting documentation contain same.

203	$5,702.00	$5,702.00	$5,702.00
208	$5,702.00	$5,702.00	$5,702.00
Total Credit	$28,644.00	$28,644.00	$28,644.00

Joint Ex. Nos. 14 through 17.

19. Applicant designated each of these particular condominiums "low income units" (hereinafter "LIUs") and rented same only to households having incomes that met the federal low income standards. Joint Ex. No. 1.

20. Applicant rented the sixth unit (Number 213) at market-rate rent. The aforementioned federal tax documents fail to disclose that KMLP claimed a Low-Income Housing Credit for this particular unit. Joint Ex. Nos. 1, 14 through 17.

CONCLUSIONS OF LAW:

An examination of the record establishes that this applicant has not submitted evidence and argument sufficient to warrant exempting the subject parcels from 1994 real estate taxes. Accordingly, under the reasoning given below, the Department's determinations that said parcels do not qualify for exemption under Public Act 88-660 and 35 **ILCS** 200/15-65 should be affirmed. In support thereof, I make the following conclusions:

Article IX, Section 6 of the Illinois Constitution of 1970 provides as follows:

> The General Assembly by law may exempt from taxation only the property of the State, units of local government and school districts and property used exclusively for agricultural and horticultural societies, and for school, religious, cemetery and charitable purposes.

The power of the General Assembly granted by the Illinois Constitution operates as a limit on the power of the General Assembly to exempt property from taxation. The General Assembly may not broaden or enlarge the tax exemptions permitted by the Constitution or grant exemptions other than those authorized by the Constitution. Board of Certified Safety

Professionals v. Johnson, 112 Ill.2d 542 (1986). Furthermore, Article IX, Section 6 is not a self-executing provision. Rather, it merely authorizes the General Assembly to confer tax exemptions within the limitations imposed by the Constitution. Locust Grove Cemetery of Philo, Illinois v. Rose, 16 Ill.2d 132 (1959). Moreover, the General Assembly is not constitutionally required to exempt any property from taxation and may place restrictions or limitations on those exemptions it chooses to grant. Village of Oak Park v. Rosewell, 115 Ill. App.3d 497 (1st Dist. 1983).

Pursuant to its Constitutional mandate, the General Assembly enacted the Property Tax Code, 35 **ILCS** 200/1 *et seq*. The omnibus provisions of that statute which govern the instant proceeding are found in Section 200/15-65. In relevant part, that provision states as follows:

> All property of the following is exempt [from real estate taxation] when actually and exclusively used for charitable or beneficent purposes, and not leased or otherwise used with a view to profit:
>
> (a) institutions of public charity.

The General Assembly amended Section 200/15-65 via enactment of Public Act 88-660. This provision, effective September 16, 1994, provides, in relevant part, that property otherwise qualifying for exemption under Section 200-15/65 shall not lose its exemption because the legal title is held:

> … (ii) by an entity that is organized as a partnership, in which the charitable organization, or an affiliate or subsidiary of the charitable organization, is a general partner, for the purposes of owning and operating a residential rental property that has received an allocation of Low Income Housing Tax Credits for 100% of the dwelling units under Section 42 of the Internal Revenue Code of 1986.[8]

8. 26 U.S.C.A. § 42.

Both the applicant and the Board posit that this case should be decided under the above amendment. However, this argument fails to recognize that "[t]he status of the property for taxation and the liability to taxation [is] fixed on [January 1 of year], and property subject to taxation on assessment day in any year is liable for the taxes of that year even though it may subsequently, during that [same] year, become exempt from taxation." Forest Preserve of DuPage County v. Department of Revenue, *et al*, 266 Ill. App.3d 264, 274 (2nd Dist. 1994) (citing People ex. rel. Kassabaum v. Hopkins, 106 Ill.2d 473, 476-77 (1985)).

Public Act 88-660 did not become effective until *after* January 1, 1994. Consequently, the above principle mandates that the amendment does not govern whether the subject parcels are exempt from that year's real estate taxes. Therefore, said inquiry must be decided according to whether this applicant satisfies the statutory and common law requirements applicable to "institutions of public charity."

An analysis of that issue begins with recognition of the following rules of statutory construction, which our courts have consistently applied in property tax cases: first, a statute exempting property or an entity from taxation must be strictly construed against exemption, with all facts construed and debatable questions resolved in favor of taxation (People ex. rel. Nordlund v. Home for the Aged, 40 Ill.2d 91 (1968)); second, the party seeking exemption bears the burden of proof (Metropolitan Sanitary District of Greater Chicago v. Rosewell, 133 Ill. App.3d 153 (1st Dist. 1985)); and third, such party can not obtain exemption unless it presents clear and convincing evidence of conformity with all applicable statutory and common law requirements therefor. (*Id*)

In this case, the appropriate exemption applies to "institutions of public charity." Our courts have long refused to apply this exemption absent suitable evidence that the property in question is owned by an "institution of public charity" and "exclusively used" for purposes which qualify as "charitable" within the meaning of Illinois law. Methodist Old People's Home v. Korzen, 39 Ill.2d 149, 156 (1968) (hereinafter "Korzen"). They have also ascribed to the following definition of "charity[,]" originally articulated in Crerar v. Williams, 145 Ill. 625, 643 (1893):

> ... a charity is a gift to be applied consistently with existing laws, for the benefit of an indefinite number of persons, persuading them to an educational or religious conviction, for their general welfare - or in some way reducing the burdens of government.

The Illinois Supreme Court has effectuated this definition by observing that all "institutions of public charity" share the following "distinctive characteristics[:]"

1) they have no capital stock or shareholders;

2) they earn no profits or dividends, but rather, derive their funds mainly from public and private charity and hold such funds in trust for the objects and purposes expressed in their charters;

3) they dispense charity to all who need and apply for it;

4) they do not provide gain or profit in a private sense to any person connected with it; and,

5) they do not appear to place obstacles of any character in the way of those who need and would avail themselves of the charitable benefits it dispenses.

Korzen at 157.

In applying these requirements to the present case, it must be remembered that KMCA, IILC and KMLP are three separate legal entities. Furthermore, although the Department has recognized KMCA and IILC as "institutions of public charity[,]" it has yet to bestow that status on the applicant. Thus, while KMCA and IILC are general partners in KMLP, they are not the applicant herein. Nor do they hold legal title to the subject properties. Accordingly, the rules requiring strict statutory construction mandate that these parcels can be exempted *only if* KMLP *itself* satisfies all of the pertinent statutory requirements. For the following reasons, I conclude it does not.

The Agreement of Limited Partnership (Joint Ex. No. 1) establishes that both the general and limited partners have capital accounts. More importantly, the First Amendment to the Agreement (Joint Ex. No. 5) provides evidence that applicant assigned 99% of the limited partner's interest to a non-exempt, for-profit corporation on January 31, 1989.

This entity, Midwest Electronics, Inc, was (per the Amendment) vested with the right to sell its interest in the subject property or make a charitable gift thereof. The Amendment expressly makes such sale subject to the condition that the real estate continue to be occupied by a low income household. However, this condition does not terminate Midwest's capacity to profit from the enterprise by claiming appropriate tax credits as long as it maintains its limited partnership interest.

The schedule K-1s attached to federal tax returns (Joint Ex. Nos. 14 through 16) demonstrate that Midwest claimed both income losses and tax credits as a result of maintaining its limited partnership interest during the 1990, 1991 and 1992 federal tax year. This evidence is technically irrelevant to the present case because it does not pertain to the 1994 assessment year. However, it does establish a pattern which, when coupled with the rules compelling inferences that support taxation and requiring that any doubts be resolved in favor of same, must be interpreted as proving that Midwest claimed such losses and credits, and thereby profited from the enterprise during 1994. Consequently, I conclude that applicant's organizational and financial structure did not conform to an "institution of public charity" in that year. Therefore, the Department's determinations denying exemption to each of the six subject parcels exemption from 1994 real estate taxes should be affirmed.

The subject properties would not be exempt even if this case were to be decided under Public Act 88-660. This provision requires that: (1) the property must "otherwise qualif[y]" for exemption under Section 200/15-65 (viz. be owned by an "institution of public charity" and be used for exempt purposes); (2) legal title to the subject property must (at least for present purposes) be held by (a) an entity that is organized as a partnership (b) in which the charitable organization, or an affiliate or subsidiary of same (c) is a general partner; (3) and which partnership functions for purposes of owning and operating a residential rental property that (4) has received an allocation of Low Income Housing Tax Credits for 100% of the dwelling units under Section 42 of the Internal Revenue Code of 1986.

The subject properties do not satisfy at least two of the above requirements: first, they do not "otherwise qualif[y]" because applicant's organizational and financial structure does not conform to that of an "institution of public charity[;]" and second, the following considerations lead me to conclude that said properties did not satisfy the statutory allocation requirements during 1994.

The stipulation fails to disclose whether applicant in fact obtained an appropriate allocation of Low Income Housing Tax Credits for the 1994 assessment year. Applicant also did not include its 1994 federal tax return in the supporting documentation. Absent this evidence, applicant has failed to prove that it satisfied the statutorily-mandated allocation requirements during the tax year currently under review.

Furthermore, applicant's federal returns for the 1991, 1992 and 1993 tax years demonstrate a very consistent pattern of obtaining allocations for only 5 of the 6 units currently at issue. While these returns are technically irrelevant to the present case, the aforementioned pattern implies that applicant consistently did not obtain allocations for all six units. Therefore, it did not satisfy the statutory requirement of operating a residential rental property that received an allocation of Low Income Housing Credits "for 100% [or *all*] of the dwelling units" during 1994.

The subject properties also do not qualify for exemption under the above criteria because one of the units is rented at market rate, and therefore, not eligible for an appropriate allocation of Low Income Housing Tax Credits. More importantly, because this unit is rented at market rate, it is primarily used to produce income for the applicant. Illinois courts have consistently held such an inherently commercial use to be non-exempt, even where the applicant devotes any income derived therefrom to an exempt purpose. <u>People ex. rel. Baldwin v. Jessamine Withers Home</u>, 312 Ill. 136 (1924); <u>Turnverein "Lincoln" v. Board of Appeals of Cook County</u>, 358 Ill. 135 (1934); <u>Salvation Army v. Department of Revenue</u>, 170 Ill. App.3d 336, 344 (2nd Dist. 1988). As such, this unit does not "otherwise qualif[y] for exemption" under Section 200/15-65.

Our courts have recognized that partial exemptions may be granted where specifically identifiable portions of real estate are actually used for exempt purposes. <u>Illinois Institute of</u>

Technology v. Skinner, 49 Ill.2d 59 (1971) (hereinafter "IIT"). One could argue that this principle might provide a basis for exempting 5 out of the 6 units currently at issue. However, IIT was not decided under the exact statutory provision involved herein, which contains a very specific use requirement. The preceding analysis demonstrates that applicant does not satisfy that requirement for two reasons: first, only five of the six units received appropriate allocations during 1994; and second, the remaining unit was rented at market rate, and thus, neither eligible for an appropriate allocation nor in exempt use under Illinois law. Therefore, granting a partial exemption herein would effectively contradict an otherwise clear legislative directive requiring that 100% of the units be in exempt use.

Applicant seeks to defeat the preceding analysis by citing Cole Hospital v. Champaign County Board of Review, 113 Ill. App.3d 96 (4th Dist. 1983); Christian Action Ministry v. Department of Local Government Affairs, 74 Ill.2d 51 (1978) and Community Mental Health Council v. Department of Revenue, 186 Ill. App.3d 73 (1st Dist. 1989), as support for its position that the subject properties should be exempt. In each of these cases, an applicant who was not the actual titleholder sought a property tax exemption. The reviewing courts granted the exemptions noting that the facts established that the titleholder was merely an "alter ego" of the equitable owner.

These courts based their conclusions on a common thread which is not present in the present case, namely that legal or practical business realities prohibited the appellants from assuming title in their own names. They reasoned that such realities effectively prevent otherwise exempt organizations from satisfying the statutorily-imposed ownership requirements and thereby defeat the underlying policy objective of fostering charitable activity.

This case is distinguishable from those cited by applicant in that KMLP's primary obstacles to exemption do not pertain to the transactional mechanisms for obtaining equitable title. Rather, they consist of its inability to qualify as an "institution of public charity" and failure to meet the use requirements prescribed by Public Act 88-660. Moreover, the six warranty deeds (Joint Ex. No. 13) establish that, unlike the above cases, KMLP actually took title to all of the subject properties in its own name.

The deeds further establish that applicant acquired same pursuant to a series of arm's length business transactions with IILC, an inference strengthened by the fact that KMLP procured one of the subject units for the non-exempt purpose of renting it at market rate. As such, these transactions do not present the types of obstacles that the above cases ameliorated in order to avoid a chilling effect on charitable activity. For these and all the above-stated reasons, the Department's determinations denying each of the six properties exemption from 1994 real estate taxes should be affirmed.

WHEREFORE, for all the above-stated reasons, it is my recommendation that DuPage County Parcel Index Numbers 08-08-113-022, 08-08-113-001, 08-08-113-010, 08-08-113-016, 08-08-113-018 and 08-08-113-027 not be exempt from 1994 real estate taxes.

03/23/98
Date

Alan I. Marcus,
Administrative Law Judge